VZCZCXRO8697
PP RUEHDU RUEHMR RUEHRN
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ZNY CCCCC ZZH
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FM AMEMBASSY HARARE
TO RUEHC/SECSTATE WASHDC PRIORITY 2409
INFO RUCNSAD/SOUTHERN AFRICAN DEVELOPMENT COMMUNITY
RUEHUJA/AMEMBASSY ABUJA 1821
RUEHAR/AMEMBASSY ACCRA 1728
RUEHDS/AMEMBASSY ADDIS ABABA 1854
RUEHBY/AMEMBASSY CANBERRA 1131
RUEHDK/AMEMBASSY DAKAR 1488
RUEHKM/AMEMBASSY KAMPALA 1910
RUEHNR/AMEMBASSY NAIROBI 4338
RUEHGV/USMISSION GENEVA 0981
RHEHAAA/NSC WASHDC
RHMFISS/JOINT STAFF WASHDC
RUEHC/DEPT OF LABOR WASHDC
RUEATRS/DEPT OF TREASURY WASHDC
RHEFDIA/DIA WASHDC//DHO-7//
RUCPDOC/DEPT OF COMMERCE WASHDC
RUFOADA/JAC MOLESWORTH RAF MOLESWORTH UK//DOOC/ECMO/CC/DAO/DOB/DOI//
RUEPGBA/CDR USEUCOM INTEL VAIHINGEN GE//ECJ23-CH/ECJ5M//

C O N F I D E N T I A L SECTION 01 OF 03 HARARE 000044

SIPDIS

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AF/S FOR S. HILL
NSC FOR SENIOR AFRICA DIRECTOR B. PITTMAN
STATE PASS TO USAID FOR L.DOBBINS AND E.LOKEN
TREASURY FOR J. RALYEA AND T.RAND
COMMERCE FOR BECKY ERKUL
ADDIS ABABA FOR USAU
ADDIS ABABA FOR ACSS

E.O. 12958: DECL: 01/23/2018
TAGS: EFIN ECON PGOV ZI
SUBJECT: CASH CRISIS PERSISTS, DESPITE NEW NOTES

REF: A. 07 HARARE 1134

¶B. 07 HARARE 1118

Classified By: Amb. James D. McGee for reason(s): 1.4 (d)

Summary

¶1. (SBU) After a series of policy flip-flops over Zimbabwe's ongoing cash crisis, Reserve Bank of Zimbabwe (RBZ) Governor Gono released new, much higher denominated notes into the cash-starved market on January 19. The new notes and higher daily cash withdrawal limits have failed, however, to solve Zimbabwe's severe cash shortage in the face of galloping hyperinflation and a sharp fall in the value of the local currency. In addition, a fall in confidence in the banking sector and the increasing size of the informal economy will continue to fuel the demand for cash. Gono's latest policy patchwork has failed, yet again, to address Zimbabwe's much larger economic crisis. END SUMMARY.

Policy Zigzagging Over Cash

¶2. (SBU) Illustrative of Zimbabwe's economic policy chaos, RBZ Governor Gono, in a spectacular succession of policy zigzags, announced in mid-December: the withdrawal of the most commonly used and highest denomination note) the Z$200,000 bill - from circulation, allegedly to combat "cash barons"; no slashing of zeros, after all; issuance of new Z$250,000, Z$500,000 and Z$750,000 notes; and a stringent limit on daily cash withdrawals (Ref A). Less than two weeks

later, faced with obviously insufficient cash to meet transaction demand, the Governor announced in a U-turn that the Z$200,000 note would continue as legal tender until further notice.

¶3. (SBU) The cash situation improved slightly in early January after a short-lived surge in deposits of Z$200,000 notes. But by mid-month cash was once again in woefully short supply, even affecting the ability of teachers to return to the classroom at the opening of the new school term this week. At the same time, the new highest-denomination note had sunk to a value of only USD 0.15 on the parallel market for bank transfers. Under intense pressure to provide the banks with enough cash to pay out the 1000 percent civil servant salary increase agreed upon in December, Gono announced on January 16 the introduction of new Z$10 million, Z$5 million and Z$1 million notes.

¶4. (SBU) Since mid-December, Gono also introduced, then, under protest from the business community, reversed, stringent new documentation requirements on every electronic bank transfer, in an apparent effort to choke the soaring parallel foreign exchange market in bank transfers (Ref B). He also reversed a new minimum threshold for transfers, allowing, once again, any amount to be transferred electronically.

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Hyperinflation/Informalization Of Economy Driving Shortage
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¶5. (SBU) The highest denomination new note is nominally worth 50 times more than the largest note in circulation a

month ago, yet under hyperinflation its value is only about USD 1-USD 2 on the parallel exchange markets today. Gono also raised the daily cash withdrawal limit from Z$50 million to Z$500 million on January 16, but most banks, for lack of adequate cash from the RBZ, are limiting withdrawals to Z$200 million/day (the equivalent of USD 40 at the street rate). Long lines for cash persist at Harare's banks.

¶6. (C) In a presentation to CABS' (Central African Building Society) premier clients attended by Econoff on January 16, the morning before Gono announced the new notes, economic analyst John Robertson elucidated the main factors driving the cash shortage: the high transaction demand for cash that accompanies hyperinflation; a fall in public confidence in banks that was driving people out of the formal banking sector and reducing deposits; and the increased level of informalization of the economy and resultant higher demand for cash. Robertson predicted the GOZ would be unable to meet the cash requirement of the 10-fold higher civil service payroll in January.

¶7. (C) Robertson also said that bank CEOs had been summoned to the RBZ that morning to discuss, in particular, "how to get cash to disaffected soldiers" this month. In his press statement later that day, Gono said a special program would be unveiled "to bring banking services closer to our Uniformed Forces."

¶8. (C) Driving the sharp price increase, according to Confederation of Zimbabwe Industries (CZI) economist Cliff Dube, is the recent jump in the price of locally sourced inputs to production, including labor. The supply of goods is insufficient to meet local demand in part also due to the inability of companies to access foreign exchange from the RBZ to buy imported inputs. The shortage of goods is exacerbated by the National Incomes and Pricing Commission (NIPC) prohibition on firms using the parallel market exchange rate to price their products. As a result, locally produced goods are either in scant supply as production contracts, or very high-priced. In the meantime, imported goods priced at the very strong parallel market exchange rate

for bank transfers are filling shop shelves. Parliament approved a bill extending the life of the NIPC by six months last week; the Bill now awaits presidential assent.

Seasonal, Short-Lived Stabilization of Exchange Rate

¶9. (C) Gono's policy patch has not stopped the depreciation of the Zimbabwe dollar on the parallel market. While the currency actually appreciated in the first instance in December and then stabilized over Christmas, the movements had less to do with policy changes than with the expected seasonal trend. Raphael Nyadzayo, CEO of the Export Credit Guarantee Company (ECGC), explained to us that most businesses close for a long Christmas break and the demand for foreign exchange falls sharply at this time against a background of increased supply flowing in from overseas Zimbabweans. In addition, this year the cash shortage added to the low demand for foreign exchange. Together with the stringent conditions announced by Gono on bank transfers (soon after reversed), these factors contributed to the local currency's relative stability over the holiday period. However, both the cash and transfer exchange rates have surged in the last days (to Z$5 million:US$1 and Z$7 million:US$1 respectively) as demand picked up with the

reopening of most firms and the weakening of economic indicators. (NOTE: The official exchange rate remains Z$30,000:US$1. END NOTE.)

Comment

¶10. (C) The infusion of new Z$10 million notes has not done much to relieve Zimbabwe's cash problem. As Robertson noted, the transaction demand for cash is immense under the combination of hyperinflation and a growing informal market. In addition, the extension of the National Incomes and Pricing Commission's life for another six months augurs poorly for local manufacturers and retailers being able to cover their operating costs and re-ignite production. In announcing the latest new notes, Gono persisted in blaming "cash hoarders, parallel market dealers and other illegal traders" for conspiring to create the cash shortage. Whether or not he believes his own rhetoric, he seems to have recognized that the cash shortage has the potential of disaffecting the civil service and, worryingly, the armed forces. His latest patch neither solves the cash problem beyond the short term nor addresses the much larger economic crisis at hand. END COMMENT.

MCGEE